DISCUSSION PAPER PREPARED FOR MINISTERIAL ADVISORY COMMITTEE ON CO-OPERATION

EVALUATION OF LOW COST LOANS AND BUYING ADVICE PROGRAMS: A CRITIQUE

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INTRODUCTION

The analysis and findings of the EVALUATION OF LOW-COST LOANS AND BUYING ADVICE PROGRAMS (1991) is based on the assumption that credit co-operatives are outside the mainstream of credit providers.

This conclusion is implicit to the evaluation undertaken by the Ministry of Consumer Affairs of its funded low cost lending services - including the Fitzroy Carlton Community Credit Cooperative and the Macaulay Community Credit Cooperative.

The evaluation concludes that the services have not accessed significant numbers of low income people to mainstream credit providers and that they are not efficient.

This critique argues that the evaluation has failed to substantiate and verify its analysis and conclusions - including its assumptions about credit cooperatives and their role in the provision of credit. The evaluation is

also superficial in examining how low income people can access credit.

Of particular interest to M.A.C.C., is the evaluation's failure to identify and acknowledge the historical, economic and social significance of credit co-operatives.

EFFECTIVENESS

The specific objective of the low cost loans program was to improve the access of low income consumers to credit.

Despite this, the evaluation persists in asking whether the low cost loans program not only achieved "the general objectives of increasing the access of low income consumers to credit" but also whether it influenced " mainstream credit providers to be more responsive to the needs of low income people..." (p 5)

Critical to these questions are definitions of "increasing the access" and "mainstream credit providers". Yet, the evaluation does not acknowledge that there is a legitimate choice of definitions and, instead, relies on implicit definitions.

The evaluation comments, for instance, that: The broad goals of CCP and the objective of low-cost loans programs have rested on the Social justice principles of access and equity. However, the Low-cost Loans program has not been effective in increasing access to credit on an equitable

basis....over the four and a half years to December 1990 loans were provided to only 1,262 pensioners and beneficiaries and 748 other low income people, at a total cost to the ministry of $455,917," (p 8)

While it is noted that the "broad goals" and "the objective" of the low cost loans services "have rested on the Social justice principles of access and equity" there is no subsequent analysis of how the services have reflected and reinforced these goals and objectives. Given that the program was developed to provide practical social justice outcomes for people who have low incomes, it is puzzling why social justice is rhetorically dismissed as a context to rather an element of the evaluation.

The evaluation has defined "increasing access to credit" as "increasing access to credit on an equitable basis." The capacity to be equitable is not only subject to what is meant but also the resources available which predetermine equitable opportunities and outcomes. Having introduced the concept of an "equitable basis" there is no attempt to define its nature and scope - other than generalised references to numbers of low income borrowers and geographical populations. What could have been equitable between people who have low incomes and people who have higher incomes has been interpreted as equitable between people who have low incomes.

The program was never required to and was incapable of providing loans on an equitable basis to all people who have low incomes in specified geographical locations. This would be a desirable long-term goal for a State-wide low cost lending service. In the meantime, it is inappropriate to criticise the services for not achieving what is unachievable - particularly in retrospect.

The evaluation does not provide information on the credit history of borrowers from the low cost lending services and, in particular, their credit rating. Yet, if the experience of these borrowers results in an improvement in their credit ratings, this is a measure of "increasing access" to credit. Establishing eligibility for credit is as important as borrowing from mainstream credit providers.

The evaluation concludes that the program has failed to access low income people to mainstream credit providers and suggests that in CREDIT TO THE COMMUNITY (1991) Chalmers and Prosser's "continuing claim" that people who have low incomes "are denied access to mainstream credit suggests that the low-cost loans program has not achieved its objective of influencing mainstream credit providers. The large number of multiple loans provided to clients is further evidence that the agencies' clients are not necessarily using low-cost loans services as a stepping stone to lending from mainstream credit providers." (p 10) Yet, the evaluation admits that the objective of influencing

mainstream credit providers to be more responsive to the needs of low income consumers was not "actually" an objective of the low-cost loans program. Incidentally, the evaluation makes the mistake of imputing to the authors of CREDIT TO THE COMMUNITY the views of the Brotherhood of St Laurence.

There is an assumption in this analysis - that the low cost lending services are outside the mainstream of credit providers. The evaluation had earlier concluded that there was no evidence that people who have low incomes were excluded by mainstream credit providers. But, then, the evaluation offered no evidence that people who have low incomes are included by mainstream credit providers. Of course, this issue is also dependent on who is defined as a mainstream credit provider. Subsequently, the Community Credit Network has met with Mr Allan Cullen, from the Australian Bankers Association, who is reported to have confirmed that banks did not issue loans for under $2,000 because of the costs of processing and administering such loans. A major Australian bank has also admitted that it is not economical to provide small loans. Evidence that people who have low incomes are excluded by banks from receiving credit does exist - in these admissions of the banks.

It is further reaffirmed by the Evaluation that the Brotherhood "Report notes that low -cost lending can assist low income people to progress from loans for coping with

financial crises, to loans for consumer products. This occurs through the development of skills in money management and applying those skills in dealing with lending institutions. This suggests that the Low-cost Loans program aims to enable loan recipients to move to mainstrezm credit providers. However, the Report presents insufficient evidence that this has occurred." (p 11)

This argument repeats the assumption that credit unions, in particular, are not mainstream credit providers and that low cost lending services, including credit co-operatives, should and must be "stepping stones" to "mainstream credit providers" i.e., banks. This "stepping stone" may be the achievement of a credit rating - rather than borrowing from banks. Furthermore, there are people who choose to join and borrow from credit cooperatives - rather than banks. For some people the democratic member-owned and controlled credit co-operatives are preferred to the shareholder owned and controlled banks.

In its NBFI's REGULATORY REVIEW CONSULTANCY (1989) KPMG Peat Marwick concluded that: NBFI's account for a significant proportion of the financial markets, both in the State of Victoria and Australia." Credit cooperatives are mainstream credit providers. At the 30 June 1989, for instance, 2,785,000 Australians were members of credit unions - representing 16.63% or one in six of the population. Credit union lending is largely concentrated in the

personal/consumer finance sector e.g., motor vehicles, home appliances, education and holiday travel.

EFFICIENCY

The evaluation has concluded that: The program has not been found to be cost effective. The evaluation examined the four funded groups and found that the interest savings to loan recipients over the period of the program has been operating were actually less than the costs of administering the program. Interest savings were based on the difference between the actual interest rate charged and credit cards and finance company interest rates." (p 14) It is noted that: In total only 1,262 pensioners and beneficiaries received loans, with total interest savings of $125,233 - $230,040, These benefits were provided at a total cost to the Ministry of #455,917." (p 15)

Yet, the evaluation's own figures suggest that this overview is misleading and is subject to different interpretations. It is conceded, for instance, that if all loans are taken into account the total interest savings is between $297,908 - $510,700. This is an outcome which would result in cost efficiency. Furthermore, the Fitzroy Carlton Community Credit Cooperative was almost cost efficient in its loans to pensioners and beneficiaries as defined by the evaluation - with funding of $138,563 and interest savings of $126,711. If all the Fitzroy co-operative's loans were taken into account, then, the maximum savings is $214,245. With

Macaulay Community Credit Co-operative if all loans were taken into account - funding of $170,835 has a maximum interest savings of $270, 296. These figures need to be understood in the context of the evaluation's assumption that if the interest rates are greater than the funding, then, the program could be considered cost-effective.

The evaluation's conclusion about cost-effectiveness has the virtue of simplicity - that the costs (the funding) are greater than the claimed relevant benefits (interest savings). While the evaluation uses the term cost-effectiveness, it is really an exercise in cost-efficiency. Beyond the debatable use of these figures, however, the evaluation does not include all the relevant costs and benefits.

The evaluation is not a cost-benefit analysis. It would have been appropriate to identify the relevant benefits and costs. What should have been included in a relevant cost benefit analysis would have been the following:

The cost to borrowers who could not obtain loans from other sources.

The cost to borrowers who could not obtain loans from other sources.

The cost to borrowers who defaulted on loans obtained from other sources.

The cost to borrowers of using services not based on problem solving and financial management.

The explicit identification of a relevant time period over which costs and benefits are assessed.
The number of borrowers who have or will havean improved credit rating.
The previous and current credit history of borrowers.
The number of potential borrowers who have been diverted into savings accounts.
The change in cost-efficiency over the four and a half year period of the program.

Quite obviously, these factors have been excluded by the evaluation because (a) the absence of appropriate data (b) the difficulties of measuring outcomes and (c) the need for a considerable time lag between costs and benefits.

The evaluation has admitted, however, that "an assessment of the impact of subsidised loans" is difficult because "there is insufficient information to guage whether the consumer would have purchased the good in the absence of a subsidised loan or could have afforded the higher interest rates." (p 10) This statement needs to be juxtapositioned with the evaluation's previous argument that there is insufficient evidence that people who have low incomes do not have access to mainstream credit providers. It is also conceded that "there may be non-financial benefits" (p 14) of the services.

The evaluation suggests that "The promotion of savings as a more viable option for agency clients" because "Given that

most of the loans made by the agencies are small, and generally well below $1,000, this is an option which should be considered fully." (p 12)

This argument assumes that people who have low incomes should defer the purchase of goods and save the purchase price - instead of accessing mainstream credit providers. In WHEN THE PRESSURE IS REALLY ON (1986), Jenny Trethewey has concluded that "low income families often have no choice but to enter into credit arrangements and pay more for consumer goods. When their level of income does not allow for savings and they have no savings reserves, this is the only means by which they can obtain such goods." (p 55) Trethewey reported that at least 70% of 49 households "consistently replied that they saved either nothing or amounts under $10 during the monitored fortnight."(p 51)

CONCLUSION

The Evaluation of Low-Cost Loans and Buying Advice programs is an inadequate and incomplete assessment of the services. The evaluation is ahistorical in not recognising that credit co-operatives established in Victoria since 1953 have been low cost lending services.

The concept of using Government funds to access banks to people who have low incomes is an interesting assumption. An alternative approach would have been to build on the credit

cooperative movement - as alternative but mainstream financial institutions.

It is suggested that the specific issue of accessing low income people to credit should be examined - building on the actual experience of the Program and the established credit co-operative movement. Of course, this assumes a community development approach - not a concept relevant to those who imagine that theory is reality and that power bestows insight. The economic rationalist might, instead, prefer to develop a clever model which is dominated by a "friendly" profit-making bank.

In CREDIT TO THE COMMUNITY (1991) Chalmers and Prosser suggest that "the community credit co-operatives are emerging as suitable models for the design of partnership projects providing affordable and consumer-oriented credit services, supported by a combination of state government and community sector funds, offering a range of financial services to their members, operating within a framework of regulatory control, and with close links to a range of other consumer support services." (p 69)